NO. 2959

IN THE

United States Circuit Court of Appeals

FOR THE

NINTH CIRCUIT.

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CITY OF BOZEMAN, a Corporation, JOHN A. LUCE, Mayor of the City of Bozeman, and C. A. SPIETH, City Clerk of the City of Bozeman,

Appellants,

vs.

SWEET, CAUSEY, FOSTER & COMPANY, a Corporation, JAMES N. WRIGHT & COMPANY, a Corporation, and C. W. McNAIR & COMPANY, a Corporation,

Appellees.

BRIEF OF APPELLEES

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BRIEF OF APPELLEES

The facts are correctly stated in the brief of Appellants. It may be necessary in the course of the argument to refer to additional facts, but such reference will be made when attention is called to them.

The lower court held that the notice of election should have submitted the proposition as to whether

the three per cent debt limit should be extended or exceeded for the purpose of issuing the bonds. In this we submit that there was no error. While the particular question here presented has not been directly involved in the cases before the Supreme Court of Montana, the language of the Constitutional and Statutory provisions is so plain and unequivocal and the purpose of these provisions to protect the taxpayer so apparent, that there is not much room for argument.

Section 6, Art. XIII of the Constitution quoted in Appellants' brief fixes the limit of indebtedness to be contracted by a city *in any manner* at three per cent.

"Provided, however, that the legislative assembly may extend the limit mentioned in this section, by authorizing municipal corporations to submit the *question* to a vote of the taxpayers affected thereby," when such increase is necessary to construct a sewerage system or procure a water supply. It is plain from this Constitutional provision that the question to be submitted is the extension of the limit of indebtedness, not the manner of creating the debt. No other authority is conferred upon the legislative assembly to extend the limit than is to be found within this section, and unless it is found here it does not exist.

But it will be noted that the Legislative Assembly, when enacting laws to carry this provision into effect, also took into consideration the method or manner of creating the debt. Section 3259, Sub-div. 64

of Rev. Codes 1907, involves several subjects of legislation, as will be apparent if we print the section in paragraphs. It provides as follows: City Councils shall have power

"64. To contract an indebtedness on behalf of a city or town, upon the credit thereof, by borrowing money or issuing bonds for the following purposes, to-wit: erection of public buildings, construction of sewers, bridges, waterworks, lighting plants, supplying the city or town with water by contract, the purchase of fire apparatus, the construction or purchase of canals or ditches and water rights for supplying the city or town with water, and the funding of outstanding warrants and maturing bonds;

provided, that the total amount of indebtedness authorized to be contracted in any form, including the then existing indebtedness must not, at any time, exceed three per centum of the total assessed valuation of the taxable property of the city or town, as ascertained by the last assessment for State and County taxes.

PROVIDED, that no money must be borrowed on bonds issued for the construction, purchase or securing of a water plant, water system, water supply, or sewerage system, until the proposition has been submitted to the vote of the taxpayers affected thereby of the city or town and the majority vote cast in favor thereof, and,

FURTHER PROVIDED, that an additional indebtedness shall be incurred, when necessary,

to construct a sewerage system or procure a water supply for the said city or town which shall own or control said water supply and devote the revenue derived therefrom to the payment of the debt: The additional indebtedness authorized, including all indebtedness heretofore contracted, which is unpaid or outstanding, for the construction of a sewerage system, shall not exceed ten per centum over and above the three per cent, heretofore referred to, of the total assessed valuation of the taxable property of the city or town as ascertained by the last assessment for State and county taxes;

and, PROVIDED FURTHER, that the above limit of three per centum shall not be extended, unless the question shall have been submitted to a vote of the taxpayers affected thereby and carried in the affirmative by a vote of the majority of said tax-payers who vote at such election."

The first paragraph confers upon City Councils the power to contract an indebtedness by borrowing money or issuing bonds for eight distinct purposes. The second paragraph carries into effect the constitutional provision of Section 6 that the total amount of the indebtedness contracted *in any form* must not exceed three per cent of the taxable property. The third paragraph provides that *no bonds* must be issued for securing a water plant or constructing a sewer until the *proposition* has been submitted to a vote of the taxpayers. The fourth paragraph authorizes an *additional* indebtedness, when necessary

to secure a water plant or sewerage system, with two qualifications, viz: the city must own the water system and devote its revenues to the payment of the debt, and the *additional* indebtedness including all indebtedness theretofore contracted must not exceed ten per cent of the valuation of the taxable property, over and above the three per cent above referred to. And lastly it is positively provided "that the above limit of three per centum shall not be extended, unless the *question* shall have been submitted" to the taxpayers. As the court below says in his opinion:

> "The question that the Statute directs shall be submitted is not, shall the city incur a bonded debt, but is, shall the city incur a bonded debt extending or exceeding the three per cent limit. To vote for the first is not to vote for the last." (Rec. p. 75).

The principle here expressed was involved in the case of Carlson vs. City of Helena, 39 Mont. 104, 102 Pac. 39, a case cited by Appellants counsel, and the opinion presents the most exhaustive discussion of these constitutional and statutory provisions. That case, however, is chiefly valuable because it presents a correct method of submitting the question.

In the Ordinance calling the special election referred to in the Carlson case the purposes of the special election are described as follows:

"Section 1. That a Special Election be held in the city of Helena on the 25th day of April, 1908,

for the purpose of ascertaining the will of the tax payers, to be affected thereby, and that authority may be given and power conferred upon the City Council to increase the indebtedness of said City over and above the three per cent limit fixed by law, by the issuance," of the bonds described therein. It will be noted that the purpose of the election is defined to be specifically the determination of the will of the tax payers upon the question that authority be given to the City Council to increase the indebtedness of the City over and above the three per cent limit. In the case at bar in the notice of election no intimation is given with reference to either the Sewer or Water Works Bonds that the indebtedness of the City was to be increased above the three per cent limit.

In the Carlson case the Court was not called upon to determine whether or not the question of exceeding the three per cent limit should be submitted, because that proposition was submitted in specific terms. The contention in that case turned upon the question as to whether authority to incur an indebtedness included an authority to issue bonds. The Court held that it did. It does not follow, however, from this decision that a reverse statement of this proposition would be true, namely that authority to issue bonds involve authority to incur an indebtedness in excess of the three per cent limit. The Legislature has declared that "no money must be borrowed on bonds issued for the construction, purchase or securing of a water plant, water system,

water supply or sewerage system, until the *proposition* has been submitted to the vote of the taxpayers affected thereby." (Rev. Codes 3259). In the same section, it also provides that the limit of three per cent shall not be extended until that *question* shall have been submitted. When the question submitted is, as was the case at bar, merely the issuance of bonds, the presumption is that the bonds are within the three per cent limit. Issuance of bonds is a matter of creating a debt and whether bonds or warrants shall be issued is not prescribed by the Constitution. Issuance of bonds in excess of the three per cent limit is the exercise of a special power which the Constitution says can be exercised only when specific authority is conferred.

The case of Arnold vs. Miles City, 46 Mont. 481, 128 Pac. 915, cited in Appellants' brief, did not present the questions here involved at all. There the bond issue before the Court was one for the construction of a bridge, a purpose which did not need a submission to the voters for authority to issue bonds. The question involved is very clearly stated by the Court to be whether a City, after having necessarily and legally incurred an outstanding indebtedness for a water supply or sewer system, under the ten per cent limit, can thereafter incur an additional indebtedness under the three per cent limit for building a bridge, the existing indebtedness of the city, incurred under the three per cent limit having fallen below that limit by reason of payments made thereon. The indebtedness is re-

quired by the Statute to come within the three per cent limit. Whether bonds or warrants were issued for that purpose was entirely within the discretion of the City Council, if there was any room for the amount within the three per cent limit. How the question of extending the limit for the water supply or sewerage system was submitted does not appear from the report of the case. But the statement of facts prepared by Judge Smith says "It was necessary at the time the indebtedness was incurred to resort to the 10 per cent limit in order that the city might acquire a water plant and sewerage system, and the bonded indebtedness of $225,000 was duly and regularly incurred for those purposes." So that, the language quoted by counsel from the opinion of Judge Smith, at page 10 of his Brief, was clearly obiter as regards the method of submission.

The case of Kerlin vs. City of Devils Lake, 141 N. W. 756, cited by Appellants might well be disposed of by reference to the case of Carlson vs. City of Helena, *supra*. But we take the liberty of calling the court's attention to the fact that the official ballot in the Kerlin case, like that in the Carlson case, specifically stated that the purpose was to increase the indebtedness and to issue bonds of the city in an amount equal to three per cent "over and above the five per cent limit of indebtedness." The language of the opinion cited by Counsel in his brief on page 15 was, to say the least, inapt.

The case of City of Oxnard vs. Bellat, 130 Pac. 701, is also of no weight as authority upon the ques-

tion here involved, for the reason that the extension of the debt limit was not present, but only the question as to whether a vote to issue bonds was a vote to create an indebtedness for the amount of the bonds.

Reference is made in the brief to Section 3454 of Rev. Codes 1907. An examination of that section discloses that it is merely declaratory of powers already conferred. If it has any bearing upon the question at issue here, it illustrates the fact that the legislature always had in mind a distinction between issuing bonds or contracting an indebtedness.

So that, we respectfully submit that the court below did not err in its interpretation of the Statutory and Constitutional provisions of Montana.

BONDS WERE VOID BECAUSE CREATING AN EXCESSIVE INDEBTEDNESS, EVEN THOUGH AUTHORIZED AFTER PROPER SUBMISSION OF QUESTION.

Assuming, however, that the court erred in holding that the question of the extension of the debt limit was not properly submitted, the action of the Court in ordering the certified checks delivered up for cancellation, was justified because the facts showed, that while the issue of Sewer Bonds would be within the ten per cent limit, the issue of $135,000 of new Water Works bonds would be beyond the ten per cent limit. The two issues were offered as one at the sale. The bids were made and accepted for

both issues. The contract provides for the return of the checks if either issue is declared invalid, and therefore must be treated as an entirety and the sale declared to be void, if the two issues are not both valid.

The illegality of the proceedings were assailed in the Bill of Complaint upon the following grounds: (Tr. p. 18)

> "(a) That at the time of the submission of the question of the issuance of said bonds to the taxpayers affected thereby, said City of Bozeman was indebted in excess of three per cent of the taxable value of the property of said City as the same appeared upon the assessment roll of said city for the year 1915, which fact will more fully appear by reference to the financial statement of said city attached hereto and heretofore referred to as 'Exhibit E'; that the question of extending the limit of indebtedness of said city for the purpose of procuring a water supply or the construction of sewers in excess of the three per cent limit of the taxable property and within the limit of ten per cent of the taxable property, as provided by the Constitution of the State of Montana, was never submitted to the taxpayers affected thereby.
>
> "(b) That the issuance of the $235,000.00 of Water Works Bonds and $70,000.00 of Sewer Bonds would in fact increase the indebtedness of said city beyond the thirteen per cent limit of indebtedness as fixed by the Constitution of the State of Montana, assuming that the question of extending the limit of indebtedness be-

yond the three per cent limit had been properly submitted to the taxpayers.

"(c) That the question of the issuance of the $235,000.00 of Water Works Bonds, of which $100,000.00 were to be used for funding bonds and $135,000.00 for the construction of additions to the water supply, was a double question, and was submitted to the taxpayers of said city as one question, and that the taxpayers affected thereby were never permitted the opportunity of expressing their will upon the two separate questions."

The plaintiff offered in evidence the financial statement, "Exhibit E", attached to the Bill of Complaint (Tr. p. 44) the delivery of which to the plaintiffs as preliminary to their bid on the bonds was admitted in the answer, and the correctness of the recitals therein contained was testified to by the City Clerk. From this statement it appears that the taxable property of the City of Bozeman, as shown by the assessment roll for the year 1915, being the last assessment roll prior to the sale of the bonds, was $3,209,196.00. Three per cent of this amount would be $96,275.88; ten per cent of this amount would be $320,919.60. The statement also showed the outstanding indebtedness of the City at the close of business March 31st, 1916, as follows, to-wit:

Water Bonds	$100,000.00
City Hall Bonds	21,000.00
Re-funding Bonds	166,000.00
Floating Indebtedness	975.00
TOTAL INDEBTEDNESS	$287,975.00

The City also had on hand cash applicable to the redemption of the bonds amounting to $6,172.38, which amount ought perhaps to be deducted from the amount of the total indebtedness, but in view of the other circumstances surrounding the case, it is immaterial whether this amount be deducted or not. If the issue of Re-funding Bonds, aggregating $166,000.00, are a valid outstanding indebtedness of the City, then the City, at the time of the attempt to issue the bonds in controversy, had exceeded the limit of three per cent referred to in the Constitution and statutes of the State of Montana, because it appeared upon the trial that this was an issue of bonds made in 1914 for the purpose of funding outstanding general warrants of the City, no part of which had been expended for water or sewer purposes.

The City contended that this issue of re-funding bonds took up outstanding warrants all of which had been issued at a time when the City had exceeded its limit of indebtedness for general purposes, and that therefore the total amount of this issue must be excluded from the computation of the limit of indebtedness to be applied in determining the validity of the bonds in controversy in this action, leaving

only the general indebtedness of the City, amounting to $21,000.00. The plaintiffs contend that the City is estopped from asserting the invalidity of the issue of re-funding bonds. Evidence was introduced on the trial to sustain the fact that the warrants for which the funding bonds were issued were all issued at a time when the City had exceeded its constitutional limit, and therefore the bonds would be invalid if the City were not estopped from raising that question.

In the financial statement submitted to the plaintiffs as preliminary to their bid, these recitals appear: "No previous issues of bonds have been contested * * * there is no controversy or litigation pending or threatened affecting * * * the validity of these bonds." The City Clerk testified (Tr. p. 122) that he made the statement containing these recitals, and that he believed them to be true when made, and that there was no record in the office of the City Clerk which would show the contrary of them. He also testified that he had in his possession as City Clerk the record of the proceedings of the City Council resulting in the issue of the series of re-funding bonds. He also had in his possession the original ordinance fixing the form of those bonds, and that ordinance contained the following clause:

> "It is hereby certified and recited that this bond is issued in strict compliance with and in conformity to the laws and constitution of the State of Montana, and that all acts, conditions

> and things required to be done precedent to the issuance of this bond have been properly and legally done, had and performed, and the full faith and credit of said City are hereby irrevocably pledged to the payment of this bond, according to its terms."

The question then arises, was the City estopped by these recitals from asserting the invalidity of the issue of re-funding bonds. This subject has received the attention of the Courts in many cases, but we are not left without authoritative decisions for the reason that the Supreme Court of the United States has fully covered the subject in several cases, which are leading cases upon the questions involved. In the case of Buchanan vs. Litchfield—102 U. S. 278—in an action by a holder of bonds to recover the amount of unpaid interest coupons attached to certain bonds issued by a municipal corporation in the State of Illinois, the rights of the holder of such bonds were presented to the Court. Mr. Justice Harlan, delivering the opinion, said:

> "In determining whether the constitutional limit of indebtedness has been exceeded by a municipal corporation, an inquiry would always be necessary as to the *amount of taxable property* within its boundaries. Such inquiry would be solved, not by information derived from individual officers of the municipality, but only in the mode prescribed in the Constitution; that is, by reference to the last assessment for state and county taxes for the year preceeding the issue of the bonds." * * * "But in what way

was the purchaser to ascertain the extent of the City's indebtedness existing at the time the bonds in question were issued? The extent of that indebtedness was a fact peculiarly within the knowledge of the constituted authorities of the City. It was necessarily left, both by the Constitution and the Statute of 1873, to their examination and determination, under the constitutional injunction, however, that no municipal corporation should exceed the prescribed amount of indebtedness. It was, nevertheless, a fact which, so far as we are advised by the record, could not, at all times and absolutely or with reasonable certainty, be ascertained from any official documents to which the public had access. A like difficulty, perhaps, would arise in the case of any municipal corporation, possessing the general power of raising money, by taxation and otherwise, to carry on local government. Its liabilities might frequently vary in their aggregate amount, and at particular periods might be of different kinds, some fixed and absolute, while others would be contingent upon events thereafter to happen. These considerations were, doubtless, present in the minds as well of those who framed the Constitution as of those who passed the Statute of 1873.

"As, therefore, neither the Constitution nor the Statute prescribed any rule or test by which persons contracting with municipal corporations should ascertain the extent of their 'existing indebtedness', it would seem that if the bonds in question had contained recitals which, upon any fair construction, amounted to a representation upon the part of the constituted authorities of

> the City that the requirements of the Constitution were met, that is: that the City's indebtedness, increased by the amount of the bonds in question, was within the Constitutional limit, then the City, under the decisions of this Court, might have been estopped from disputing the truth of such representations as against a bona fide holder of its bonds."

In the Litchfield case it was held that inasmuch as the bonds in controversy contained no recitals of compliance with the constitutional requirements, the City was not estopped from raising that objection. But in the case of Gunnison vs. E. H. Rollins, 173 U. S. 689—the question was presented to the Supreme Court in an action on an issue of bonds which recited full compliance with the constitutional requirements. The Supreme Court, again speaking by Mr. Justice Harlan, reviews very fully not only the case of Buchanan vs. Litchfield, but several later cases in that Court, including the case of Chaffee County vs. Potter—142 U. S. 355—In both the Gunnison and Chaffee cases the constitutional provision of the State of Colorado was involved, and doubtless the Court is aware that it has been asserted that our constitutional provisions have been taken from Colorado. After reviewing severally the authorities, Mr. Justice Harlan thus concludes:

> "It was expressly decided in the Chaffee case that the statute under which the bonds there in suit (the bonds here in suit being of the same class) authorized the county commissioners to determine whether the proposed issue of bonds

> would in fact exceed the limit prescribed by the Constitution and the statute; and the recital in the bond to the effect that such determination had been made and that the constitutional limitation had not been exceeded, taken in connection with the fact that the bonds themselves did not show such recital to be untrue, estopped the county, under the law, from saying that the recital was not true. We decline to overrule Chaffee County vs. Potter, and upon the authority of that case, and without re-examining or enlarging upon the grounds upon which the decision therein proceeded, we adjudge that as against the plaintiff the county of Gunnison is estopped to question the recital in the bonds in question, to the effect that they did not create a debt in excess of the constitutional limit, and were issued by virtue of and in conformity with the statute of 1881, and in full compliance with the requirements of law."

So that we think that it is the settled rule of the Supreme Court of the United States that where municipal bonds recite upon their face full compliance with the constitutional and statutory requirements of the state of their issuance, the municipality estopped from asserting the invalidity of such issue as against such bonds in the hands of a bona fide holder. We are unable to find any case which deals with the right of an intending bidder to rely upon the recitals of the records in declining to complete his bid. But if the purchaser of the series of refunding bonds had the right to rely upon the recitals of the records of the City of Bozeman with reference

to these bonds, and if those bonds are by reason of said recitals valid outstanding obligations of the City in the hands of third persons who are not parties to this litigation, it is difficult to conceive upon what ground this Court would impose a greater duty with reference to such recitals upon an intending purchaser of a later series of bonds than it could impose upon the purchaser in an action in this Court upon the re-funding bonds themselves. On the contrary, it seems to us that the Court will hold that the intending bidder was entitled to rely upon the recitals of those records as to the validity of the re-funding bonds in attempting to determine the amount of the outstanding indebtedness of the City. A person in law is only bound to know the facts which might be ascertained upon inquiry into the transaction indicated. We therefore submit that for the purpose of this suit, the issue of re-funding bonds was an "indebtedness heretofore contracted which is unpaid or outstanding" within the provisions of sub-section 64, section 3259, Revised Codes of Montana, 1907, and that the City had no authority to issue any of the bonds in controversy without first submitting to the vote of the taxpayers the question of extending the limit of indebtedness beyond three per cent, and had no authority to issue such bonds, even after a vote of the people, where the aggregate of the indebtedness, outstanding and authorized, exceeded the ten per centum over and above the three per centum limit. That this issue did so exceed the limit is shown by a statement of the condition of the

indebtedness with the bonds in controversy issued.

Existing Indebtedness, including $100,000.00 Water Works Bonds		$287,975.00
Sewer Bonds		70,000.00
TOTAL		$357,975.00
New Water Works Bonds		135,000.00
TOTAL		$492,975.00
3% Taxable property	$ 96,275.88	
10% Taxable property	320,919.60	417,195.48
Excess of Water Bonds		$ 75,779.52

SUBMISSION OF A DOUBLE QUESTION.

The notice of the election for the issuance of the Water Works Bonds, however, submitted as one question the issuance of Refunding Bonds and New Bonds. This presented to the tax payers a double question which could not be submitted in one and the same ballot.

Stern vs. Fargo, 26 L. R. A. (N. S.' 665;

Blaine vs. Hamilton, 116 Pac. 1076, 35 L. R. A. (N. S.) 577;

Tullock vs. City of Seattle, 124 Pac. 481;

Lobough vs. Cook, 127 Iowa 181;

McBryde vs. City of Montesana, 34 Pac. 559.

In the last case cited the identical question here involved, viz: the submission of a proposition to fund old debts and borrow money for future purposes was presented and held to be the submission of two propositions in one ballot, which was improper. Upon the general question of the divisability of questions and the necessity of giving to the voter an opportunity to express an opinion upon each, reference is made to the case of the State ex rel Hay vs. Alderson, 41 Mont. 385.

We therefore respectfully submit that the action of the Court below should be affirmed.

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